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Is It Law or Something Else?: A Divided Judiciary in the Application of Fraudulent Transfer Law under § 546(e) of the Bankruptcy Code

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Where two groups of identical subjects are presented with the same set of stimuli, and they respond differently, an explanation is needed. Further, when the subjects do not merely respond randomly, but rather in one of two specific ways, this need for explanation becomes more apparent. In this Note, I will focus on the divide between bankruptcy judges and federal appellate judges in their interpretation of § 546(e) of the Bankruptcy Code,[1] as applied to leveraged buyouts in bankruptcy, in the determination of whether creditors may use fraudulent conveyance law to recover funds for the bankruptcy estate.

My position is that there is a defined and radical difference in interpretation of § 546(e), commonly known as the 'settlement payment exception,' as between bankruptcy judges and the federal appellate judges reviewing these decisions.[2] In order to explore this divergence, I conducted an empirical study to determine the existence and magnitude of this division based on the court opinions within each federal circuit. My goal was first to describe this division and then to explain why bankruptcy judges and federal appellate judges have adopted such radically different positions. A review of all of the § 546(e) case law demonstrates that eighty-six percent of federal appellate judges hold that a trustee may not use fraudulent conveyance law to avoid transfers made to shareholders in the context of a leveraged buyout as a result of §

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1. 11 U.S.C. §§ 101-1532 (2012) ("Bankruptcy Code"). Unless otherwise indicated, all further section references are to the Bankruptcy Code.

2. The study excluded district court decisions because there was no clear trend of interpretation of § 546(e). The data are current as of August 2014.

546(e).[3] By comparison, only thirty-seven percent of bankruptcy judges autonomously hold that a trustee may not use fraudulent conveyance law as a result of § 546(e).[4] This means that sixty-three percent of bankruptcy judges hold that § 546(e) does *not* apply to protect payments made to shareholders in the context of a leveraged buyout. Certainly, the different positions taken by bankruptcy judges and federal appellate judges cannot be justified merely by the statutory language. Although all judges use formal legal reasoning as a vehicle to explain the outcomes, the difference in outcomes must mean that there are other, unarticulated factors driving these decisions.

In Part I of this Note, I will provide a general overview of leveraged buyouts. The discussion of how and why LBOs are implemented is particularly relevant to the application of fraudulent transfer analysis. In Part II, I will discuss fraudulent transfer law as defined by the Bankruptcy Code. In Part III, I will discuss which transfers within the LBO should be attacked under fraudulent transfer law and why; this section will focus on the various stakes of the parties involved in the leveraged buyout transaction. I will provide an overview of the specific factors that bankruptcy and federal appellate judges may or may not consider in applying § 546(e). Part IV will then more thoroughly define § 546(e) and its application to fraudulent transfer analysis. In Part V, I will describe the split of interpretation of § 546(e) as demonstrated by an empirical study. In Part VI, I will discuss the formal legal rules for the disagreement among the bankruptcy and federal appellate judges. Finally, in Part VII, I propose several explanations for the remarkably divided application of the statute.

I. What is an LBO?

A leveraged buyout ("LBO") is a corporate acquisition that is financed through the use of debt.[5] In the most basic form of the transaction, a purchasing entity ("Acquirer") finances the purchase of a

3. *See infra* Appendix I. 12/14 (86%) appellate decisions held that § 546(e) applied.

4. *See infra* Appendix I. 10/27 (63%) autonomous bankruptcy decisions held that § 546(e) applied.

5. *See* Anthony Michael Sabino, *Applying the Law of Fraudulent Conveyances to Bankrupt Leveraged Buyouts: The Bankruptcy Code's Increasing Leverage over Failed LBOs*, 69 N.D. L. REV. 15, 20 (1993).

target corporation ("Target") by using the Target's assets to secure a loan from a lending institution ("Lender").[6] The loan from the Lender is then used to purchase the shares of stock from the Target's stockholders, thereby transferring ownership of the Target to the Acquirer.[7] Through these means, "investors convert much of the equity of the corporation into debt, cash out the prior stockholders at a premium, and gain control of a highly leveraged corporation."[8]

The increasing popularity of the leveraged buyout structure is a result of the financial feasibility of acquisition;[9] there is a minimal capital requirement where the majority of the purchase price is financed by borrowing against the assets of the Target.[10] Therefore, "[w]hen credit is cheap and the economy is growing, highly leveraged buyouts represent the optimal means by which private equity firms acquire target companies."[11] However, as is typical of any corporation operating with a high debt to equity ratio, even a slight change in economic conditions can pose a significant risk of bankruptcy to the Target.[12] Given the

6. *See id.*; *see also* David Gray Carlson, *Leveraged Buyouts in Bankruptcy*, 20 GA. L. REV. 73, 74 (1985); Emily L. Sherwin, *Creditors' Rights Against Participants in a Leveraged Buyout*, 72 MINN. L. REV. 449, 449 (1988).

7. *See* Sherwin, *supra* note 6, at 450. This structure represents the archetypical LBO. Although there are many variations of the archetypical form, the transaction remains substantively the same. *See* Neil M. Garfinkel, Note, *No Way Out: Section 546(e) is No Escape for the Public Shareholder of a Failed LBO*, 1991 COLUM. BUS. L. REV. 51, 53 (1991) ("There are many variations upon this basic transaction scenario, but in each of them, the acquired company's debt to equity ratio has increased, and its number of shareholders has usually decreased.").

8. Raymond J. Blackwood, Note, *Applying Fraudulent Conveyance Law to Leveraged Buyouts*, 42 DUKE L.J. 340, 342 (1992).

9. *See* Michael Simkovic & Benjamin S. Kaminetzky, *Leveraged Buyout Bankruptcies, the Problem of Hindsight Bias, and the Credit Default Swap Solution,* 2011 COLUM. BUS. L. REV. 118, 128-30 (2010); *see also* Samir D. Parikh, *Saving Fraudulent Transfer Law*, 86 AM. BANKR. L.J. 305, 305 (2012) (noting that within the most recent decades "[p]rivate equity firms [have come to] rely on leveraged buyouts in order to acquire target companies.").

10. Minimal liquidity is required where the security interest permits "borrow[ing] an amount that represents approximately 60 to 90 percent of the purchase price." Parikh, *supra* note 9, at 311.

11. Parikh, *supra* note 9, at 307; *see* Simkovic & Kaminetzky, *supra* note 9, at 124 ("During the credit boom that started in 2003 and peaked in 2007, banks issued a remarkable volume of loans and bonds, and an astounding volume of highly leveraged transactions were financed.").

12. *See* John H. Ginsberg et al., *Befuddlement Betwixt Two Fulcrums: Calibrating the Scales of Justice to Ascertain Fraudulent Transfers in Leveraged Buyouts*, 19 AM. BANKR. INST. L. REV. 71, 75 (2011) ("As the Third Circuit put it, '[t]he problem universal

recent liquidity crisis[13]—and the corresponding credit crunch[14]—it is not difficult to imagine that servicing this debt burden became difficult for many corporations.[15] For this reason, "[t]he problem universal to all LBOs—characterized by their high debt relative to equity interest—is that they are less able to weather temporary financial storms because debt demands are less flexible than equity interest."[16] Arguably, the LBO structure has caused many corporations to file for bankruptcy in recent years.[17]

The leveraged buyout is a prime example of a 'high risk, high reward' business transaction. Although the debt incurred as a result of the acquisition often leaves minimal cash flow for continued Target operations, the utility of the LBO is based on the future expected benefit to the Acquirer rather than an immediate increase in wealth of the Target. The Acquirer stands to profit considerably from its ability to successfully restructure the Target—typically an underperforming or undervalued corporation—and later sell it at a premium.[18] The Acquirer maximizes the return on its corporate knowledge and expertise by replacing Target management, restructuring the firm's assets, and utilizing the synergies

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13. *See* Michael D. Bordo, *An Historical Perspective on the Crisis of 2007-2008* 2 (Nat'l Bureau of Econ. Research, Working Paper No. 14569, 2008), *available at* http://www.nber.org/papers/w14569.pdf (discussing how the international financial crisis began with liquidity issues in the U.S.).

14. Brian Cheffins & John Armour, *The Eclipse of Private Equity*, 33 DEL. J. CORP. L. 1, 1 (2008).

15. In the wake of the liquidity crisis, the number of Chapter 11 filings has consistently increased each year. The comparative percent changes indicate 29.7%, 33.3%, and 27.4% increases for the years 2008, 2009, 2010 respectively. *See Table F: U.S. Bankruptcy Courts—Bankruptcy Cases Commenced, Terminated and Pending During the 12-Month Periods Ending March 31, 2009 and 2010*, U.S. COURTS.GOV, http://www.uscourts.gov/uscourts/Statistics/BankruptcyStatistics/BankruptcyFilings/2010/0310_f.pdf (last visited Apr. 11, 2014).

16. Ginsberg et al., *supra* note 12, at 75 (quoting *Mellon Bank*, 945 F.2d at 647).

17. *See* HEINO MEERKATT & HEINRICH LIECHTENSTEIN, BOS. CONSULTING GRP., GET READY FOR THE PRIVATE-EQUITY SHAKEOUT: WILL THIS BE THE NEXT SHOCK TO THE GLOBAL ECONOMY? 1, 3-4 (Dec. 2008), http://www.iese.edu/en/files/PrivateEquityWhitePaper.pdf; *see also* Anthony Michael Sabino, *supra* note 5, at 36; Nelson D. Schwartz, *Corporate Debt Coming Due May Squeeze Credit*, N.Y. TIMES, Mar. 16, 2010, at A1, *available at* http://www.nytimes.com/2010/03/16/business/16debt.html?pagewanted=all&_r=0.

18. Carlson, *supra* note 6, at 79.

between the Target and other firms owned by the Acquirer.[19] "If the corporation is able to pay off the LBO debt . . . [the Acquirer] enjoy[s] huge profits . . . hav[ing] purchased full equity participation in a successful company with a small expenditure of [its] own funds."[20] Therefore, in the context of the fraudulent transfer analysis, it should be noted that it is typically the potential profitability of the Target that motivates the acquisition, rather than actual intent to defraud.[21]

II. Fraudulent Transfer Law

Given the high risk to the Target as a result of the enormous debt burden,[22] a substantial number of these acquisitions result in bankruptcy.[23] Fraudulent transfer law becomes relevant to these corporate bankruptcies when, in light of the priority of distribution of assets in bankruptcy, the overwhelming secured claims of the Lender leave little to no potential of recovery for unsecured creditors.[24] "The purpose of fraudulent transfer law is to prevent a debtor from transferring away valuable assets in exchange for less than adequate value, if the transfer leaves insufficient assets to compensate honest creditors."[25] Therefore, where the Target "is left in inadequate financial condition following a buyout and later fails, unpaid creditors may assert claims against parties who participated in the buyout," perhaps most effectively through the use of fraudulent conveyance statutes.[26] If the transactions

19. *See* James F. Queenan, Jr., *The Collapsed Leveraged Buyout and the Trustee in Bankruptcy*, 11 CARDOZO L. REV. 1, 10 (1989); *see also* Myron M. Sheinfeld & David H. Goodman, *LBO: Legitimate Business Organization or Large Bankruptcy Opportunity?*, 2 J. BANKR. L. & PRAC. 799, 800-01 (1993).

20. Blackwood, *supra* note 8, at 342.

21. *See* Kupetz v. Wolf, 845 F.2d 842 (9th Cir.1988) ("We cannot believe that virtually all LBOs are designed to 'hinder, delay, or defraud creditors.'"). As such, fraudulent transfer analysis in this context is typically centered on constructive fraud. However, it should be noted that actual intent to defraud, while tremendously difficult to prove, typically defeats the § 546(e) affirmative defense. *See* 11 U.S.C. § 546(e) (2012) (excluding actual fraud by reference to § 548(a)(1)(A)).

22. *See* Parikh, *supra* note 9, at 307.

23. *Id.* at 308; *see* Schwartz, *supra* note 17.

24. *See* Stephen E. Schilling, *Ambiguity and Bad Policy: Should § 546(e) of the Bankruptcy Code Be Applied to Leveraged Buyouts of Private Companies?*, 9 DEPAUL BUS. & COM. L.J. 471, 478 (2011).

25. *In re* Bay Plastics, Inc., 187 B.R. 315, 322 (Bankr. C.D. Cal. 1995) (citations omitted).

26. *See* Sherwin, *supra* note 6, at 452.

within the LBO fall within the statutory definition of a fraudulent conveyance,[27] the transactions are subject to avoidance and funds may be brought back into the bankruptcy estate for the benefit of unsecured creditors.[28]

The legal bases for avoiding the LBO transfer as a fraudulent conveyance are embodied in the Bankruptcy Code; either directly through the operation of § 548[29] or through § 544(b),[30] which permits a Trustee[31] to use state legislation, including the Uniform Fraudulent Conveyance Act ("UFCA"), in a minority of states, and the Uniform Fraudulent Transfer Act ("UFTA"), in a vast majority of states, to avoid the transaction.[32]

Section 548 of the Bankruptcy Code permits the avoidance of both actually fraudulent and constructively fraudulent transfers within two years prior to the date the bankruptcy petition is filed.[33] A transfer may be avoided under § 548(a)(1)(A) where the Trustee can prove actual fraud on the part of a party who makes a transfer or incurs an obligation with "actual intent to hinder, delay, or defraud."[34] However, proving actual intent can be difficult given the general business objectives of the Acquirer in conducting the LBO.[35] Alternatively, § 548(a)(1)(B) provides an opportunity for a Trustee, on behalf of the class of unsecured

27. There is ongoing debate as to whether fraudulent conveyance law should apply in the context of a leveraged buyout. *See* Blackwood, *supra* note 8, at 350 ("[B]ecause fraudulent conveyance laws arose out of a simplistic and outdated sixteenth-century setting, applying such laws to transactions as modern and complex as the LBO is wholly inappropriate.").

28. *See* Sherwin, *supra* note 6, at 464 ("The remedy provided to creditors, or to a bankruptcy trustee [or debtor in possession] on creditors' behalf, is to avoid the transfer and recover the property or its value from transferees [for the bankruptcy estate]."); *see also* 11 U.S.C. § 548(a) (2012); Schilling, *supra* note 24, at 478.

29. 11 U.S.C. § 548.

30. *Id.* § 544(b).

31. In a Chapter 11 bankruptcy, the debtor in possession may exercise all the rights of the trustee, aside from the right to receive compensation. *Id.* § 1107(a). "Trustee" will hereinafter encompass both a trustee and debtor in possession.

32. A Trustee may invoke the Bankruptcy Code, relevant state law, or both. *See* Garfinkel, *supra* note 7, at 53-56.

33. 11 U.S.C. § 548.

34. *Id.* § 548(a)(1)(A).

35. Proving actual fraud also entails a higher evidentiary burden. *See* Garfinkel, *supra* note 7, at 56 ("Because of the difficulty of proving scienter, however, most trustees have sought to avoid the leveraged buyout through the constructive fraud provisions."). It should, however, be noted that proof of actual fraud would render § 546(e) inapplicable. *See* 11 U.S.C. § 546(e).

creditors, to prove constructive fraud in order to avoid the transfer.[36] A transfer of property or obligation incurred is constructively fraudulent if, *inter alia*, the debtor "received less than a reasonably equivalent value in exchange for such transfer or obligation; and . . . was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation."[37]

In addition, a Trustee can invoke state fraudulent conveyance law under § 544(b)(1) of the Bankruptcy Code, which permits a Trustee to "avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law."[38] As in the case of § 548(a)(1)(A), proof of actual fraud under state law requires "actual intent to hinder, delay, or defraud."[39] However, for the same reasons stated above, actual intent is exceedingly difficult to prove. Alternatively, proof of constructive fraud requires analysis under a two-pronged test.[40] Under the first prong, the Trustee must demonstrate that the transfer was not made for "fair consideration" (under the UFCA)[41] or that it was not made for a "reasonably equivalent value" (under the UFTA).[42] Where the first prong is satisfied, the court must then determine whether "the debtor was either (a) insolvent at the time of the transaction or rendered insolvent by the transaction,[43] or (b) left with

36. *Id*. § 548(a)(1)(B).

37. *Id*.

38. *Id.* § 544(b)(1). *But cf. In re* Lyondell Chem. Co., 503 B.R. 348, 355 (Bankr. S.D.N.Y. 2014) (holding that § 546(e) does not apply to lawsuits brought under state fraudulent transfer laws).

39. *See* UNIF. FRAUDULENT TRANSFER ACT § 4(a)(1), 7A U.L.A. 58 (2006) (internal quotation marks omitted).

40. *See* Kevin J. Liss, Note, *Fraudulent Conveyance Law and Leveraged Buyouts*, 87 COLUM. L. REV. 1491, 1497 (1987).

41. *See* UNIF. FRAUDULENT CONVEYANCE ACT § 3, 7A U.L.A. 277 (2006). The National Conference of Commissioners on Uniform State Laws no longer publishes the UFCA. However, the basic structure and approach of the UFCA are preserved in the UFTA. Only five states (including New York) still utilize the UFCA. *See, e.g.*, N.Y. DEBT. & CRED. LAW §§ 270-81 (McKinney 2014); *see also* Blackwood, *supra* note 8, at 362-63 (Under the UFCA fair consideration analysis, where the "purpose of fraudulent conveyance law is to protect creditors from unwarranted depletion of the debtor's assets, the sufficiency of the consideration is viewed from the perspective of the LBO target's creditors."). For the New York provision for "fair consideration" see, N.Y. DEBT. & CRED. LAW § 272.

42. *See* UNIF. FRAUDULENT TRANSFER ACT § 4(a)(2), 7A U.L.A. 58 (2006).

43. *See* Liss, *supra* note 40, at 1497 & n.42 (citing UNIF. FRAUDULENT CONVEYANCE ACT § 4, 7A U.L.A. 474 (1985); UNIF. FRAUDULENT TRANSFER ACT § 5(a), 7A U.L.A. 657 (1985)).

unreasonably small capital."[44] Where both prongs have been met, the transfer can be avoided and the funds brought back into the bankruptcy estate.[45]

III. Which Are the Alleged Fraudulent Transfers Subject to Avoidance?

A. *Which Transfers Should be Attacked?*

The analysis of this multiparty transaction within the scope of fraudulent conveyance law is especially difficult where fraudulent conveyance statutes were drafted to address a standard two-party transaction.[46] Within the context of an LBO, the application of fraudulent transfer law requires a determination of which transfers should be avoided, and therefore recovered by the estate for the benefit of creditors. Although this analysis may be affected by the specific structure of the LBO,[47] courts have found that certain payments made by a debtor either to the Lender or to the selling shareholder may be avoided.[48] Therefore, the two major foci of the fraudulent transfer analysis within the archetypical leveraged buyout include the lender-target mutual obligations and payments to selling shareholders.

In the most basic form of the LBO, the Lender typically makes a loan in exchange for a security interest in the assets of the Target, as directed by the Acquirer. Where the loan funds are deposited directly with the Target, the Target appears to have incurred a clear obligation (to repay the loan), and at first glance, appears to have received a reasonably equivalent value (the loan proceeds). However, both the Target's assumption of the obligation to repay the loan and the Target's transfer of a security interest in its assets to the Lender are potentially fraudulent transfers.[49] Although the Target's assets have been pledged to secure

44. *Id.* at 1497 & n.43 (citing UNIF. FRAUDULENT CONVEYANCE ACT § 5, 7A U.L.A. 504 (1985); UNIF. FRAUDULENT TRANSFER ACT § 4(a)(2)(i), 7A U.L.A. 652 (1985)).

45. *Id.* at 1497.

46. 11 U.S.C. § 548(a)(1)(B) (2012); *see also* Daniel J. Merrett & John H. Chase, *Safe Harbor Supernova: Is Section 546(e)'s Stellar Protection of Private LBO Transactions About to Burn Out*? 21 J. BANKR. L. & PRAC. 3 Art. 1, n.161 (2012).

47. For further discussion of this topic, see *infra* Part VII.B.

48. *See* Sabino, *supra* note 5, at 26. For a discussion of the collapsing doctrine, see *infra* Part VII.B.

49. There is also the argument that payments to selling shareholders may be deemed fraudulent on the theory that Target management authorized the overpayment for

repayment of the loan, the loan funds received immediately flow through the Target to selling shareholders; the Target does not beneficially retain the loan proceeds.[50] Rather, the Target appears to act as a mere conduit as distributor of funds to the selling shareholders at the direction of the Acquirer. The implications of this structured transaction will be discussed in Part V, *infra*.

B. *Why Should the Transfer be Avoided?*

The purpose of applying fraudulent transfer law in order to employ the avoidance powers is to "level the playing field among similarly situated creditors[,] . . . to maximize the amount of property available to a debtor's general unsecured creditors[,]"[51] and to facilitate the success of the reorganization. However, the question then becomes, why level the playing field among creditors? Why protect the unsecured creditors at all? This is the root of the divide between bankruptcy judges and federal appellate judges and will be discussed in Parts VI and VII, *infra*. However, to understand the arguments that perpetuate this divide, one must first consider the circumstances of the players involved in, and affected by, the LBO.

1. Target Shareholders

First, recall that prior to the leveraged buyout the Target was identified by the Acquirer as an underperforming corporation. It seems inequitable that the Target shareholders should receive priority in corporate distribution when they would have been residual claimants in the bankruptcy in the absence of the LBO. Furthermore, these shareholders have not only been paid for their shares, but also have been paid at a premium despite having assumed absolutely no risk.[52] "The selling shareholders receive their price at closing and have no continuing stake in the target, and thus no exposure to risk of leverage-induced

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outstanding shares (at a premium) despite the apparent financial infeasibility, evidenced by the resulting bankruptcy. *See* Parikh, *supra* note 9, at 308. This argument will not be explored in this Note.

50. *See* Carlson, *supra* note 6, at 75.

51. Merrett & Chase, *supra* note 46.

52. *See* Queenan, *supra* note 19, at 5.

insolvency."[53] Therefore, there is an impropriety where, "in anticipation of a liquidation, shareholders extract value from the company at a time when the general creditors have not been paid."[54]

2. Secured Creditor

Lenders, on another hand, are protected by their security interests and have "voluntarily assume[d] credit-risk in pursuit of commensurate interest rates providing a favorable risk-adjusted return."[55] Lenders can "scrutinize the transaction before entering into it[] . . . [and] respond by increasing the price—the interest rate—charged for credit because of the increased risk of fraudulent conveyance attack."[56] Therefore, the Lender is in the best position to foresee the bankruptcy where it has the opportunity to analyze the current financial state of the Target[57] prior to issuance of the loan. The Lender may then take corresponding precautions, such as adjusting the interest rate and structuring the transaction to protect its own interests in the event of a bankruptcy. Conveniently enough, the security interest in the collateral provides the Lender with priority of distribution in the bankruptcy estate.[58]

3. Acquirer

The Acquirer obviously draws various financial benefits from the LBO where the potential profit is what motivates the acquisition. Where the Acquiring management is able to manage successfully the operations of the newly acquired Target so as to produce a profit, debt can be paid off and Acquiring management enjoys a corresponding increase in the value of its equity.[59] Additionally, where the "the buyout dramatically

53. Ginsberg et al., *supra* note 12, at 76.

54. Carlson, *supra* note 6, at 85.

55. Ginsberg et al., *supra* note 12, at 76.

56. Liss, *supra* note 40, at 1513.

57. Depending on the structure of the transaction, the Lender may also analyze the financial state of the Acquirer as well. *See generally* Carlson, *supra* note 6, at 81-83 (discussing different forms of LBOs).

58. 11 U.S.C. § 507 (2012); *see also* Irina V. Fox, *Settlement Payment Exception to Avoidance Powers in Bankruptcy: An Unsettling Method of Avoiding Recovery from Shareholders of Failed Closely Held Company LBOs*, 84 AM. BANKR. L.J. 571, 575 (2010).

59. *See* Ginsberg et al., *supra* note 12, at 77.

narrows the ownership base, any appreciation in the company's equity is thereby divided among fewer parties."[60] In the event that Acquiring management is not able to successfully produce a profit as a result of the overwhelming debt burden, the resulting loss is limited by the fact that the financing for the LBO came from a loan secured by the assets of the Target; little to no equity necessarily has been lost.[61] The "worst case scenario for [Acquiring management] is that they will lose their market investment in the LBO if they are unable to sell their position before the [T]arget's failure."[62]

4. Unsecured Creditor

Therefore, unsecured creditors assume the risk of the bankruptcy associated with the LBO. This is the definition of being unsecured, and therefore holds true whether there is an LBO or not. However, where the positive net worth of the Target has been reduced by the secured debt, the Lender's priority secured liens additionally minimize, if not eliminate, the recovery potential for these unsecured creditors. Of course, there are both sophisticated and unsophisticated unsecured creditors. Yet, while the sophisticated unsecured creditors typically manage bankruptcy risk by charging risk adjusted interest rates or negotiating bond covenants, unsophisticated, unsecured creditors have little knowledge or access to information, and ultimately, have no bargaining power.[63] Where the majority of unsecured creditors are unsophisticated, the application of fraudulent conveyance law may be especially appropriate where these individuals "are poorly positioned to limit such risk, not being party to the LBO and being unshielded by any good proxy among the parties."[64]

Under the Bankruptcy Code and state law, courts have an effective

60. Parikh, *supra* note 9, at 313 (citing Garfinkel, *supra* note 7, at 52-53); *see also* Queenan, *supra* note 19, at 1.

61. "Most important to the acquiring group . . . is the gradual increase in their equity in the target. As the income stream repays the debt, the controlling group's investment becomes less and less leveraged." Garfinkel, *supra* note 7, at 53. However, the inference is that where the income stream is unable to repay the massive debt incurred by the Target, as evidenced by the resulting bankruptcy, the Acquirers have little to no equity to lose.

62. Fox, *supra* note 58, at 580.

63. *See* Liss, *supra* note 40, at 1512.

64. Ginsberg et. al., *supra* note 12, at 75.

tool to avoid fraudulent transfers in order to protect the interests of creditors of the bankruptcy estate. There is substantial case law that demonstrates that courts have used these tools frequently to maximize the recovery for the estate in liquidation and reorganization. Yet remarkably, the Bankruptcy Code includes a provision that leads some judges to hold that fraudulent transfer law is inapplicable to fraudulent transfers made in the context of an LBO.

IV. Settlement Payment Exception

Section 546(e) of the Bankruptcy Code has changed the application of fraudulent transfer law in the context of an LBO. Within the past few decades,[65] what was once "a relatively obscure section of the U.S. Bankruptcy Code"[66] is now a commonplace defense to creditor suits known as the 'settlement payment exception.' The 'settlement payment exception' exempts from avoidance various transfers made during the buyout by precluding a Trustee from using § 548, or state law (the UFCA or UFTA) through § 544(b) to recover property for the benefit of the estate. Section 546(e) provides that:

> (e) Notwithstanding sections 544 . . . 548(a)(1)(B), and 548(b) of this title, the trustee may not avoid a transfer that is a . . . *settlement payment*, as defined in section 101 or 741 of this title, made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, *financial institution*, financial participant, or securities clearing agency, or that is a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency, in connection with a securities contract, as defined in section 741(7), commodity contract, as defined in 761(4), or forward contract, that is made before the commencement of the case, except under section

65. *See* Schilling, *supra* note 24, at 473.
66. Garfinkel, *supra* note 7, at 51.

548(a)(1)(A) of this title.[67]

Recall from Part III that the potentially fraudulent transfers subject to avoidance include the Target's assumption of the obligation to repay the loan, the Target's transfer of a security interest in its assets to the Lender, and the contemporaneous payments made to Target shareholders.[68] What this means is that these transfers may be shielded from avoidance where any of these transfers are held to constitute a settlement payment made by (and to) a financial institution or a transfer by (and to) a financial institution in connection with a securities contract.[69] As a result, the major difficulty posed by § 546(e), at least in terms of legal formalism, results from two very different interpretations of which transfers constitute 'settlement payments' and what enterprises come within the statutory term, 'financial institution.'

The statutory definition of 'settlement payment' is exceptionally vague; it is defined only by reference to §§ 101 and 741, neither of which provides much more clarity.[70] Section 101(51A) defines settlement payment as "a preliminary settlement payment, a partial settlement

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67. 11 U.S.C. § 546 (2012) (emphasis added). The judicial interpretation of "settlement payment" differs slightly from the statutory definition and suggests that a "settlement payment" means "the transfer of cash or securities made to complete a securities transaction." *In re* Resorts Int'l, Inc., 181 F.3d 505, 514-15 (3d Cir. 1999) (citation omitted).

68. *See supra* Part III. Where the LBO structure requires that such contemporaneous payments be made to the shareholders in order to effectuate the acquisition, courts "refuse[] to characterize the loans and the buyout as separate transactions." Matthew T. Kirby et al., *Fraudulent Conveyance Concerns in Leveraged Buyout Lending*, 43 BUS. LAW 27, 42 (1987) ("The transactions were treated as one because '[t]he two exchanges were part of one integrated transaction[.]'" (quoting United States v. Tabor Realty Corp., 803 F.2d 1288, 1302 (3d Cir. 1986))). "[T]he payment to the shareholders by the buyer of the corporation is deemed a fraudulent conveyance because in exchange for the money the shareholders received they *provided no value to the corporation but merely increased its debt* and by doing so pushed it over the brink." Schilling, *supra* note 24, at 478 (quoting Boyer v. Crown Stock Distribution, Inc., 587 F.3d 787, 792 (7th Cir. 2009)) (emphasis added). The LBO is typically challenged on fraudulent conveyance grounds where funds were merely passed through the debtor, to former shareholders. Therefore, the fraudulent transfer claims are often brought against former shareholders, but can also be brought against officers and directors, lenders, and financial advisors. The issue then becomes whether there was actual or constructive intent to defraud. Sherwin, *supra* note 6, at 452.

69. *See, e.g.*, *In re* MacMenamin's Grill Ltd., 450 B.R. 414, 419 (Bankr. S.D.N.Y. 2011).

70. Zahn v. Yucaipa Capital Fund, 218 B.R. 656, 675 (Bankr. D.R.I. 1998) (suggesting that the definition of settlement payment is both "circular and cryptic").

payment, an interim settlement payment, a settlement payment on account, a final settlement payment, a net settlement payment, *or any other similar payment commonly used in the forward contract trade*."[71] Section 741(8), defines 'settlement payment' as "a preliminary settlement payment, a partial settlement payment, an interim settlement payment, a settlement payment on account, a final settlement payment, *or any other similar payment commonly used in the securities trade*."[72] As various courts have noted, this "definition of 'settlement payment' is frustratingly self-referential—essentially stating that a 'settlement payment' is a 'settlement payment.'"[73]

The definition of 'financial institution' is also subject to debate, despite having a less circular statutory definition. Section 101(22) of the Bankruptcy Code defines a 'financial institution' to include all "commercial or savings banks . . . savings and loan association[s] [and] . . . federally-insured credit union[s]," as well as other entities.[74] Similarly, Black's Law Dictionary defines a financial institution as "[a] business, organization, or *other entity* that manages money, credit, or capital, such as a bank, credit union, savings-and-loan association, securities broker or dealer, pawnbroker, or investment company."[75] The challenge is that the definition of 'financial institution' is not subject to any explicit limitation.

The conflict between bankruptcy judges and federal appellate judges arises because the definition of 'settlement payment' and the definition of 'financial institution' are not explicitly limited. The absence of definitional clarity has been an issue for to the courts to reconcile—or not reconcile—in the interpretation of § 546(e)'s application to LBOs.

V. Bankruptcy Judges v. Federal Appellate Judges

Since 1985, beginning with *In re International Gold Bullion Exchange, Inc.*,[76] sixty-three percent[77] of bankruptcy judges have

71. 11 U.S.C. § 101(51A) (emphasis added).

72. *Id*. § 741(8) (emphasis added).

73. *In re* MacMenamin's, 450 B.R. at 418 (citing *In re* QSI Holdings, Inc., 571 F.3d 545 (6th Cir. 2009)).

74. 11 U.S.C. § 101(22).

75. BLACK'S LAW DICTIONARY 706 (9th ed. 2009) (emphasis added).

76. 53 B.R. 660 (Bankr. S.D. Fla. 1985); *see also infra* Appendix I.

interpreted § 546(e) narrowly, thus limiting § 546(e)'s exemption from avoidance. That is, bankruptcy judges have consistently held that § 546(e) does not protect payments made to shareholders in the context of an LBO. Conversely, since 1990, beginning with *Kaiser Steel Corp. v. Charles Schwab & Co.*,[78] eighty-six percent[79] of federal appellate judges have interpreted § 546(e) broadly. That is, federal appellate judges have consistently held that § 546(e) prevents a Trustee from avoiding these payments.[80] The disagreement among courts in determining whether the transfer of funds in the context of an LBO is considered a 'settlement payment'[81] is obviously not random. Where some judges consistently interpret the same statute in one way and other judges consistently interpret the same statute in an opposite way, all the while using the same canons of statutory interpretation, there is a need for explanation.

A. *The Study*

Given the radically different treatment of § 546(e) by bankruptcy judges and federal appellate judges, I conducted an empirical study to determine the extent of this trend based on the court opinions within each federal circuit. My goal was first to describe this trend and then to explain why these judges have adopted such radically different positions on this issue. I analyzed the judicial decisions construing § 546(e) between 1985 and 2013,[82] although not necessarily in the context of

77. *See infra* Appendix I. 17/27 (63%) autonomous bankruptcy court decisions held § 546(e) does NOT apply.

78. 913 F.2d 846 (10th Cir. 1990).

79. *See infra* Appendix I. 12/14 (86%) appellate court decisions held § 546(e) applies.

80. "The Second Circuit recently reiterated that it follows the Third, Sixth, and Eighth Circuits, in holding that any transfer to a financial institution may qualify for protection, even if it is only serving as a conduit or intermediary." *In re* Tougher Indus., Inc., Nos. 06-12960. 07-10022, 2013 WL 5592902, at *5 (Bankr. N.D.N.Y. Oct. 10, 2013) (footnote omitted).

81. Fox, *supra* note 58, at 574 ("[T]he only common point in all circuits is that a trustee cannot recover from the market intermediaries.").

82. "In the 1980's, easy credit and the availability of junk bond financing created a frenzy of leveraged buyouts . . . ." William C. Rand, Comment, In re Kaiser Steel Corporation*: Does Section 546(e) of the Bankruptcy Code Apply to a Fraudulent Conveyance Made in the Form of an LBO Payment?*, 19 FORDHAM URB. L.J. 87, 87 (1991). For statistics on mergers and acquisitions from 1980-88, see U.S. BUREAU OF THE CENSUS, STATISTICAL ABSTRACT OF THE UNITED STATES: 1990 534 tbl.883 (1990), *available at* http://www2.census.gov/prod2/statcomp/documents/1990-05.pdf.

leveraged buyouts.[83] I will explain the reasons for the differing interpretations in Parts VI and VII, *infra*.

B. *Methodology*

For purposes of this study, I determined that § 546(e) addresses three types of transfers: 1) "a transfer that is a margin payment"; 2) a transfer that is a "settlement payment, . . . made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency"; and 3) "a transfer made by or to (or for the benefit of) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency in connection with a securities contract, . . . a commodity contract, . . . or forward contract."[84] My study focused on a subset of the second type of transfer: a transfer that is a "settlement payment made by or to (or for the benefit of) a financial institution."[85] I excluded those decisions involving the first and third types of transfers referenced above.

I conducted this study by generating a search for all cases construing the § 546(e) 'settlement payment exception.'[86] In order to ensure meaningful results, I analyzed only those decisions that dealt with the merits of fraudulent conveyance actions and the application of § 546(e) in cases in which there was a controversy as to whether the transfer in question was a 'settlement payment' made by or to a 'financial institution.' Therefore, I excluded decisions involving procedural matters and decisions in connection with procedural phases such as motions to dismiss and reviews of summary judgment. Finally, I excluded those decisions involving any transfers made by or to an enterprise that would more obviously be considered a financial institution within the securities industry, including banks, brokerage

83. The genesis of the study was inspired by the divergence of interpretation regarding the application of § 546(e) to protect the payments made to shareholders in the context of a leveraged buyout. From this analysis, a more prominent trend emerged, thereby inspiring a more generalized study. However, the resulting explanation of the data is equally applicable in the leveraged buyout context.

84. 11 U.S.C. § 546(e) (2012).

85. *Id.*

86. I generated a search on the legal search engines, Westlaw Next and LexisNexis, using the search terms: "11 U.S.C. 546(e)," "section 546(e)," and "settlement payment exception" within all state and federal courts.

firms and clearing agencies governed by SIPA[87] regulations.[88]

This methodology provided a sample size of fourteen appellate court decisions and thirty-eight bankruptcy court decisions. However, of the thirty-eight bankruptcy court decisions, I excluded eleven non-autonomous decisions. The exclusion of these decisions was guided by the principle that bankruptcy courts are legally bound by both district and federal appellate court decisions within the same circuit that are factually on point. Therefore, I use "autonomous" to describe an opinion issued by a bankruptcy judge where the judge was not bound by precedent. This was determined by classifying the holdings into two groups. The first group of autonomous bankruptcy court decisions includes cases of first impression because no prior appellate court decisions had been rendered within the circuit. The second group is comprised of those cases in which the bankruptcy judge held he or she was not bound by the precedent set by the district and federal appellate courts within that circuit. Analysis of both groups suggests that twenty-seven of the bankruptcy court decisions are autonomous.[89] The eleven non-autonomous decisions were those decisions issued by bankruptcy judges in which the judge was, willingly or unwillingly,[90] bound by precedent.[91] Although bankruptcy judges have issued the decisions, the decisions are not pertinent because they merely reiterate the binding rationale of their federal appellate court. I excluded these decisions from my analysis because they do not contribute meaningfully to the data regarding the interpretational split.

The purpose for refining the data is evidenced by the results in the Third Circuit, for example.[92] After *In re Resorts International, Inc.*[93]

87. Securities Investor Protection Act, 15 U.S.C. §§ 78aaa-78lll (2012).

88. The term 'financial institution' is extremely open-ended. *See supra* Part IV. Therefore, such exclusion was admittedly a more subjective aspect of the study.

89. *See infra* Appendix I.

90. One could argue that what looks like a non-autonomous decision is actually an autonomous decision because the bankruptcy judge has *chosen* to be bound by precedent. This would suggest that all decisions are in fact autonomous and precedent is meaningless, particularly where distinguishing facts is subject to judicial discretion. *See, e.g.*, Jerome Frank, *What Courts Do in Fact*, 26 ILL. L. REV. 645, 660 (1931) (discussing, hypothetically, how two judges may understand what the objective facts are). This would fall in line with the radical indeterminist theory. *See, e.g.*, Anthony D'Amato, *Pragmatic Indeterminacy*, 85 NW. U. L. REV. 148 (1990). I, however, am not willing to say that precedent is meaningless here.

91. *See infra* Appendix I.

92. *See infra* Appendix I, Third Circuit.

was decided in 1999, the subsequent bankruptcy court decisions in that circuit, which could not sufficiently distinguish the facts, were bound by the decision[94] and held that § 546(e) applied to protect payments made to shareholders. The general trend in the Third Circuit following *In re Resorts International, Inc.* highlights the purpose in designating certain decisions as non-autonomous; this demonstrates that the bankruptcy judges are not always able to render a decision based on their own interpretation of the scope of § 546(e).

C. *The Results*

The raw data are rather revealing. The explanatory percentages are based on a total of fourteen appellate court decisions and twenty-seven autonomous bankruptcy court decisions. Twelve of the fourteen, or eighty-six percent of, appellate judges held that § 546(e) exempted the debtor's transfers from avoidance, holding that these transfers constituted settlement payments.[95] By comparison, ten of the twenty-seven, a mere thirty-seven percent of, bankruptcy judges autonomously exempted these transfers from avoidance, holding that these transfers constituted settlement payments.[96] Thus, the disagreement among courts in determining whether the transfer of funds in the context of an LBO is considered a 'settlement payment' made by (or to) a 'financial institution' is obviously not random. One must ask the glaring question that remains, however: why is there a disagreement at all? I will provide several rational explanations in Parts VI and VII, *infra*.

VI. Does Legal Formalism Explain the Data?

In our common law tradition, when the same issue of law is posed to two different courts, the result should be the same in the absence of glaring error; "[a] single answer in most, if not all, cases can be deduced

93. 181 F.3d 505 (3d Cir. 1999).

94. This is the principle of *stare decisis*. 20 AM. JUR. 2D *Courts* § 129 (2013); *see infra* Appendix I (listing the Third Circuit cases decided after *In re Resorts International, Inc.*).

95. *See infra* Appendix I. Twelve of the fourteen appellate decisions held that § 546(e) applied.

96. *See infra* Appendix I. Ten of the twenty-seven autonomous bankruptcy decisions held that § 546(e) applied.

by judges who are able to restrict themselves to the rules and to avoid making any moral or public policy decisions in rendering judgments."[97] Therefore, it is significant when bankruptcy judges consistently interpret § 546(e) narrowly and federal appellate judges consistently interpret § 546(e) broadly.

Legal formalism "asserts that legal disputes are resolvable solely by recourse to legal rules and principles, and to the facts of each particular dispute."[98] Where judges are engaged in interpreting the same statute and have received the same formal training in the same analytical methods, it becomes clear that the 'facts of each particular dispute' must serve as the justification for this departure. Judges are bound only if a case presents the same legally relevant facts as the precedent, but of course, there is no meta-rule that informs a judge of what facts are legally relevant. As a result, almost every case can be distinguished. The question is why judges will distinguish particular cases at all. There are several possible explanations for this. The difference between the treatment of fraudulent transfers and the application of § 546(e) is a product of a number of variables which, operating in combination, explain the divergence. Under the pretense of legal formalism, judges cite the legal arguments of plain meaning and congressional intent as justification for the holdings.[99] However, the inconsistent application of the canons of interpretation suggests that something else is driving these decisions; legal formalism does not explain the outcomes.

A. *Plain Meaning: It Says What It Says*

Bankruptcy judges hold that the plain meaning of § 546(e) does not necessarily exempt private stock transactions—including payments to selling shareholders—from avoidance as constructive fraudulent

97. Michael P. Ambrosio, *Legal Realism*, NEW JERSEY LAW., Oct. 2000, at 30. *See generally* Edward Rubin, *The Real Formalists, the Real Realists, and What They Tell Us About Judicial Decision Making and Legal Education*, 109 MICH. L. REV. 863 (2011) (reviewing BRIAN Z. TAMANAHA, BEYOND THE FORMALIST-REALIST DIVIDE: THE ROLE OF POLITICS IN JUDGING (2010)).

98. Ambrosio, *supra* note 97, at 30.

99. *See* Schilling, *supra* note 24, at 484; *see also* Fox, *supra* note 58, at 573 ("The application of the settlement payment exception is problematic because of the contradiction between the broad literal wording of the exception and its narrow legislative purpose. The language of the statute is quite expansive and arguably exempts all stock transactions from avoidance, while the legislative history indicates that the statute meant to protect only the market for publicly traded stock.").

transfers.[100] As applied to an LBO, "the key language in § 546(e) is that the [T]rustee may not avoid a transfer that is a 'settlement payment' made 'by or to' a 'financial institution.'"[101] The textual support for bankruptcy judges' refusal to apply the settlement payment exception to this type of private stock transfer is based on their interpretation of the plain meaning of the statute—the "*belief* that the Bankruptcy Code's definition of 'settlement payment' is limited by the phrase '*or any other similar payment commonly used in securities trade*' that appears at the end of Bankruptcy Code section 741(8)."[102] Bankruptcy judges hold that the contemporaneous payments made to selling shareholders during the effectuation of the LBO are not payments commonly used in the securities trade, and thus, that § 546(e) does not protect the transfers to shareholders from being voided as fraudulent transfers; to hold as such "would . . . deprive the [statutory] definition of meaning."[103] Additionally, § 101(22) of the Bankruptcy Code defines 'financial institution' entities as, *inter alia*, including all commercial and savings banks, savings and loan associations, and federally insured credit unions.[104] Aside from being broad, and far from plain, this language provides for the "mere conduit" argument, encouraging the running of money through 'financial institutions' as a mere means of protecting these payments to shareholders, which are not commonly used in the securities trade, from avoidance.[105]

On the other hand, federal appellate judges, applying the same canons of statutory interpretation,[106] hold that § 546(e) has a different

100. *See In re* MacMenamin's Grill Ltd., 450 B.R. 414, 419 (Bankr. S.D.N.Y. 2011) (collecting cases); *In re* Grand Eagle Companies, Inc., 288 B.R. 484, 495 (Bankr. N.D. Ohio 2003) ("[Target] will not be permitted to merely cite to that technically drafted statutory protection mechanism to summarily defeat the Committee's claims.").

101. Schilling, *supra* note 24, at 490 (quoting 11 U.S.C. § 546(e) (2012)).

102. *In re MacMenamin's,* 450 B.R. at 421 (emphasis added) (quoting 11 U.S.C. § 546(e)); *see also* 11 U.S.C. § 741(8).

103. *In re* Norstan Apparel Shops, Inc., 367 B.R. 68, 76 (Bankr. E.D.N.Y. 2007).

104. 11 U.S.C. § 101(22).

105. *See, e.g.*, *In re* Munford, Inc., 98 F.3d 604, 610 (11th Cir. 1996) ("But the bank here was nothing more than an intermediary or conduit. Funds were deposited with the bank and when the bank received the shares from the selling shareholders, it sent funds to them in exchange. The bank never acquired a beneficial interest in either the funds or the shares.").

106. *See* Lamie v. U. S. Trustee, 540 U.S. 526, 534 (2004) ("It is well established that 'when the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms.'" (quoting Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A., 530 U.S. 1, 6

plain meaning than the plain meaning described by the bankruptcy judges.[107] This plain meaning protects all parties to the transaction at the expense of unsecured creditors because payments to shareholders within the context of an LBO are 'commonly used in the securities trade.'[108] In addition, most federal appellate judges oppose the "mere conduit" argument articulated by the bankruptcy courts.[109] These judges hold that the language of § 546(e) contains no requirement that a financial institution acquire a beneficial interest in the funds it handles.[110] This plain meaning permits the parties to run money through 'financial institutions' to prevent the possibility of avoidance if they so choose.

Where the "term 'plain meaning' implies that something is apparent on its face and incapable of reasonable disagreement,"[111] it becomes clear that the plain meaning of § 546(e) is less than plain and that other factors contribute to this divided interpretation.

B. *Congressional Intent*: *But What Does It Mean?*

Where a statute has no plain meaning, or yields absurd results, judges turn to Congressional intent to give meaning to the statutory language.[112] The legislative history of § 546(e) suggests that Congress enacted the statute in 1982 to "minimize the displacement caused in the

(2000))).

107. *See, e.g.*, Contemporary Industries Corp. v. Frost, 564 F.3d 981, 986 (8th Cir. 2009) ("[T]he relevant text has a sufficiently plain and unambiguous meaning. We agree with our sister circuits that § 741(8) was intended to sweep broadly. Thus, we conclude the term 'settlement payment,' as used therein, encompasses most transfers of money or securities made to complete a securities transaction." (citations omitted)).

108. *See In re* QSI Holdings, Inc., 571 F.3d 545, 550 (6th Cir. 2009) ("[N]othing in the statutory language indicates that Congress sought to limit that protection to publicly traded securities.").

109. *Compare In re* Quebecor World (USA) Inc., 480 B.R. 468, 476-77 (2012) ("At least three courts of appeals, however, have expressly rejected *Munford*, holding that 'the plain language of § 546(e) simply does not require a 'financial institution' to have a 'beneficial interest' in the transferred funds.'") (collecting cases), *with In re Munford, Inc.*, 98 F.3d at 610 (applying the "mere conduit" argument).

110. 11 U.S.C. § 546(e) (2012).

111. Schilling, *supra* note 24, at 516.

112. "[W]here the plain language, even if literally applicable, would yield absurd results at odds with the statutory design, courts may look beyond the printed word to the law as a whole and its purposes and policy, so as to determine what particular legislative intent may apply." *In re* Adler, Coleman Clearing Corp., 263 B.R. 406, 478 (S.D.N.Y. 2001) (citing *Massachusetts v. Morash*, 490 U.S. 107, 115 (1989)).

commodities and securities markets in the event of a major bankruptcy affecting those industries."[113] The rationale behind preventing the avoidance power of a Trustee by means of the settlement payment exception "was to prevent the bankruptcy of one party in the commodities clearance and settlement [system] from spreading to other parties," thereby threatening the collapse of the entire market.[114] However, "[a]t the time of the 1981 Subcommittee Hearings, leveraged buyouts were . . . obscure and occurred infrequently;"[115] the repercussions of preventing the avoidance powers of a Trustee in the context of an LBO were not yet considered. Therefore, there is little statutory guidance on the application of § 546(e) to prevent avoidance of payments to shareholders in the context of an LBO.[116]

Where bankruptcy judges hold that § 546(e) is not plain in meaning, they view the legislative history of § 546(e) as highly relevant to the statute's application in the context of private stock transaction,[117] noting that "[w]here a securities transaction is entirely private, such as in an LBO of a privately held company . . . it is difficult to see how the purpose of protecting the national clearance and settlement system has any relationship to that LBO."[118] Bankruptcy court opinions typically reflect the notion that the settlement payment exception, as applied to LBOs, serves no purpose in preventing "the domino effect"[119] within the commodities and securities markets.

In the absence of plain meaning, federal appellate judges also turn to congressional intent. In doing so, these judges hold "that the broad definition of settlement payment further[s] a policy of protecting

113. H.R. REP. NO. 97-420, at 1 (1982), *reprinted in* 1982 U.S.C.C.A.N. 583, 583.

114. Garfinkel, *supra* note 7, at 61-62.

115. Parikh, *supra* note 9, at 337.

116. *See id.* at 332 (citing H.R. REP. NO. 97-420).

117. *See, e.g*., Buckley v. Goldman, Sachs & Co., No. Civ.A.02-CV-11497RGS, 2005 WL 1206865, at *7 (D. Mass. May 20, 2005) ("The object that Congress sought to accomplish by enacting § 546(e) was to protect the operation of the security industry's clearance and settlement system. That interest is not furthered in any meaningful sense by bringing an LBO like the one at issue in this case under the exemption of § 546(e) simply because funds fortuitously passed through financial institutions on their way into the hands of the defendants."); *see also In re* MacMenamin's Grill Ltd., 450 B.R. 414, 419-20 (Bankr. S.D.N.Y. 2011); *In re* Norstan Apparel Shops, Inc., 367 B.R. 68, 76 (Bankr. E.D.N.Y. 2007) (interpreting H.R. REP. NO. 97–420).

118. Schilling, *supra* note 24, at 492.

119. *Bankruptcy of Commodity and Securities Brokers: Hearings Before the Subcomm. on Monopolies and Commercial Law of the H. Comm. on the Judiciary*, 97th Cong. 203 (1981) (statement of Edmund Schroeder); *see also* H.R. REP. NO. 97-420, at 1.

securities markets from harm that might occur if bankruptcy [T]rustees have the power to unwind settled securities transactions;"[120] that "interpreting 'settlement payment' to include the transfer of consideration in an LBO is consistent with the way 'settlement' is defined in the securities industry . . . [as] 'the completion of a securities transaction.'"[121] In addition, the federal appellate judges disagree with the interpretation put forth by the bankruptcy judges based on the supposition that "Congress could have addressed the breadth of § 546(e) and the definition of settlement payment, but it has not done so."[122]

Where "[i]t remains ambiguous what exactly the settlement payment exception [must] shield in order to protect the markets,"[123] it is clear that plain meaning and congressional intent are not determinative. There must be something else that perpetuates the divide between bankruptcy and federal appellate judges. Legal formalism does not explain the data.

VII. So, What Does Explain the Data? Articulating the Unarticulated

Where judges are to reason deductively from the same formal rules—plain meaning and congressional intent—and consider the same set of facts, legal formalism suggests that the outcomes should be the same. Yet, although judges say, by means of written legal opinion, that they are merely interpreting the statute,[124] the difference of interpretations is remarkable. Where bankruptcy judges have adopted a pragmatic analysis, federal appellate judges instead have adopted a purely textual analysis. The question then becomes, why? I see three possible explanations for this divide: the specialization of the bankruptcy courts, the recognition that bankruptcy courts are acting as courts of equity, and the attitudinal differences towards judicial regulation of the

120. Schilling, *supra* note 24, at 488.

121. Kaiser Steel Corp. v. Charles Schwab & Co., Inc., 913 F.2d 846, 849 (10th Cir. 1990) (quoting A. PESSIN & J. ROSS, WORDS OF WALL STREET: 2000 INVESTMENT TERMS DEFINED 227 (1983)).

122. Schilling, *supra* note 24, at 488 (citing *In re* Quality Stores, Inc., 355 B.R. 629, 634 (Bankr. W.D. Mich. 2006)).

123. Fox, *supra* note 58, at 587.

124. *See* Frank, *supra* note 90, at 653 ("Opinions . . . disclose but little of how judges come to their conclusions. The opinions are often ex post facto; they are *censored expositions.*").

private market.

A. *Impact of Specialization on Bankruptcy Court Decisions*

One argument is that court specialization has had an impact on the judiciary system. Prior to 1898, "[f]ederal bankruptcy legislation was used as a temporary and emergency measure, appropriate only to deal with the aftermath of economic downturn."[125] However, the Bankruptcy Reform Act of 1978[126] established the bankruptcy courts as specialized courts.[127] As specialized courts, bankruptcy courts have since developed considerable experience with regard to bankruptcy matters and as a result, tend to view cases pragmatically. This approach makes sense where bankruptcy judges hear only bankruptcy cases—100% of their caseload involves bankruptcy cases. In contrast, out of the 44,440 cases pending in the federal appellate courts as of March 21, 2011, only 610 of these cases involved bankruptcy matters.[128] This number of bankruptcy cases represents roughly one percent of the total caseload, divided among various judges. Bankruptcy judges may be better equipped to understand the implications of using § 546(e) to protect payments to shareholders as a result of their wealth of experience[129]: "[s]pecialist judges can be, and often are, recruited from the ranks of lawyers who have practiced in that area, so they often come to the bench with relevant expertise."[130]

125. JEFFREY T. FERRIELL & EDWARD J. JANGER, UNDERSTANDING BANKRUPTCY 112 (3rd ed. 2012).

126. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 402, 92 Stat. 2549, 2682 (1978).

127. "Specialized courts usually are defined as forums of highly limited jurisdiction to which all of the cases of a particular type are channeled." Rochelle C. Dreyfuss, *Forums of the Future: The Role of Specialized Courts in Resolving Business Disputes,* 61 BROOK. L. REV. 1, 5 (1995). Bankruptcy courts typically fall within this category. *See* Jeffrey J. Rachlinski, et al., *Inside the Bankruptcy Judge's Mind*, 86 B.U. L. REV. 1227, 1228 (2006).

128. *See Table B-1: U.S. Courts of Appeals—Appeals Commenced, Terminated, and Pending, by Circuit, During the 12 Month Period Ending March 31, 2011*, U. S. COURTS.GOV, http://www.uscourts.gov/Viewer.aspx?doc=/uscourts/Statistics/FederalJudicialCaseloadStatistics/2011/tables/B01Mar11.pdf (last visited Apr. 13, 2014).

129. *See* Fox, *supra* note 58, at 572 ("Stripping the bankruptcy trustee or debtor of avoidance powers for payments to shareholders in connection with an LBO potentially encourages poorly planned LBOs and may facilitate funneling cash away from failing companies to the detriment of the creditors." (footnote omitted)).

130. Rachlinski et al., *supra* note 127, at 1229.

Bankruptcy judges issuing decisions interpreting § 546(e) had been practicing within the bankruptcy field for an average of about twenty-nine years prior to deciding the case at hand.[131] On the other hand, federal appellate judges had spent an average of 0.75 years exclusively practicing in the bankruptcy field prior to issuing a decision in regard to § 546(e).[132] This "reflects only the practical reality that district court [and appellate court] judges are usually not much interested in bankruptcy and are overwhelmed with other litigation."[133] Although there is some criticism of court specialization,[134] "[t]he romantic view of the generalist federal judge, however, is not without its costs. Obsession with the generalist deprives the federal judiciary of potential expertise, which could be extremely useful in cases involving complex doctrines and specialized knowledge,"[135] particularly in cases construing § 546(e).

B. *Bankruptcy Courts as Courts of Equity*

The disparity of interpretation reflects the notion that bankruptcy judges typically view the transactions in terms of equity,[136] whereas the federal appellate judges view the transactions in terms of law. This may be particularly true where "[t]he function of bankruptcy courts is to implement the social policy set forth in bankruptcy law."[137] This is

131. *See infra* Appendix II.

132. *See infra* Appendix III.

133. FERRIELL & JANGER, *supra* note 125, at 130; *see* Stephen Lubben, *The Need for More Bankruptcy Knowledge on the Circuit Courts*, CREDIT SLIPS (March 30, 2010, 12:16 PM), http://www.creditslips.org/creditslips/2010/03/the-need-for-more-bankruptcy-knowledge-on-the-circuit-courts.html.

134. Rachlinski et al., *supra* note 127, at 1230 ("Here, we report evidence showing that bankruptcy judges are vulnerable to anchoring and framing effects . . . .").

135. Edward K. Cheng, *The Myth of the Generalist Judge*, 61 STAN. L. REV. 519, 524 (2008).

136. "The Supreme Court has recognized for many years that bankruptcy courts 'are essentially courts of equity, and their proceedings [are] inherently proceedings in equity.'" KENNETH N. KLEE, BANKRUPTCY AND THE SUPREME COURT 223 (2008) (alteration in original). However, there exists a strong debate surrounding origins of bankruptcy courts as courts of equity. *See, e.g.*, Marcia S. Krieger, *"The Bankruptcy Court Is A Court of Equity": What Does That Mean?*, 50 S.C. L. REV. 275, 275-76 (1999). Much of this argument centers on Bankruptcy Code § 105(a), which allows a bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." *Id*. at 307 n.208 (quoting 11 U.S.C. §105(a) (2012)).

137. Krieger, *supra* note 136, at 276.

demonstrated by the fact that, "whether by liquidation or reorganization, [bankruptcy law] serves admittedly equitable objectives."[138] To understand this explanation, one must first consider how this emphasis on equity in the bankruptcy courts came to be.

"Article III, Section 2 of the United States Constitution and the Judiciary Act of 1789, as amended, confer and delegate, respectively, *equitable authority* to federal district judges . . . ."[139] Under the Bankruptcy Acts of 1867 and 1898, district courts were defined as "courts of bankruptcy," and were given original jurisdiction in all matters and proceedings in bankruptcy.[140] Congress later repealed the Act of 1898 and replaced it with the Bankruptcy Reform Act of 1978,[141] thereby revoking the bankruptcy court's explicit powers as a court of equity.[142] Although not truly a court of equity, it is still true that "[b]ankruptcy laws, by their nature, embody a compromise between fundamental, competing social and economic objectives."[143]

There is a similar argument that bankruptcy courts are involved in the practice of legal realism. "[Legal] [r]ealists s[eek] the moral dimension in law, not in rules and principles or the higher law appraisals of rules and principles, but in the process of responsible decision."[144] This legal theory underlies the pragmatic approach of the bankruptcy judges, particularly where "legal realists consider[] . . . solutions to practical social problems[] . . . [and maintain] a common sense approach to legal analysis."[145]

Whether labeled equity or legal realism, it is clear that considerations of fairness and the potential for abuse typically trouble bankruptcy judges; these opinions often articulate that § 546(e) permits "a nominal number of shareholders to receive windfall profits at the expense of employee pension plans, retirement plans, mutual funds, and

138. *Id.*

139. Alan M. Ahart, *The Limited Scope of Implied Powers of A Bankruptcy Judge: A Statutory Court of Bankruptcy, Not a Court of Equity*, 79 AM. BANKR. L.J. 1, 12 (2005) (emphasis added) (construing U.S. CONST. art. III, § 2).

140. *See id.* at 16-19.

141. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 401, 92 Stat. 2549, 2682 (1978).

142. Ahart, *supra* note 139, at 22.

143. Krieger, *supra* note 136, at 276.

144. Ambrosio, *supra* note 97, at 34.

145. *Id.*

other entities that manage funds belonging to millions of individuals."[146] Furthermore, the majority of unsecured creditors cannot realistically protect themselves; instead, "powerful creditors will protect themselves while less advantageously situated creditors have no comparable means of protection."[147]

The notion of bankruptcy courts as courts of equity is further reflected in an equitable doctrine, known as the 'collapsing doctrine,' developed in the context of LBOs and unique to the bankruptcy courts. Where a focus of fraudulent transfer analysis is whether the transaction involved sufficient consideration, as required under § 548 or state law through § 544, a threshold inquiry in certain fraudulent transfer actions is whether the particular transactions sought to be avoided can be considered in isolation or should be considered as part of an integrated transaction.[148] The collapsing doctrine has been applied where many variations on the classic LBO have been structured in order to sidestep the fraudulent transfer analysis of the archetypical form,[149] allowing courts to avoid creative circumvention of the law.[150] The essence of this doctrine is that despite the structural variations in the LBO, the underlying transaction remains substantively the same.[151] Despite the strategic manipulation of the transactions within the LBO, "once the LBO transactions are collapsed, sufficient consideration is unlikely to be found unless concrete indirect benefits accrue for the target corporation."[152] This result provides the potential for significant

146. Parikh, *supra* note 9, at 310-11.

147. Liss, *supra* note 40, at 1512.

148. In recent years, courts have increasingly looked to the "the overall effect of the LBO on the target corporation . . . rather than the effect of each discrete transaction." Blackwood, *supra* note 8, at 362.

149. *See* Garfinkel, *supra* note 7, at 57 ("A properly structured LBO might be arranged, however, so that the individual steps of the buyout, when viewed as discrete transactions, may not be constructively fraudulent as to creditors."). These variations in structure will not be discussed in this Note. For further discussion, *see* Carlson, *supra* note 6, at 81-83.

150. *See, e.g.*, Wieboldt Stores, Inc. v. Schottenstein, 94 B.R. 488, 503 (Bankr. N.D. Ill. 1988) ("[T]he formal structure of the transaction alone cannot shield the LBO lenders or the controlling . . . shareholders from Wieboldt's fraudulent conveyance claims."). The focus is on the net effect to honest creditors. *See id.*

151. The Supreme Court has held that "a bankruptcy court, as a court of equity, may look through form to substance when determining the true nature of a transaction as it relates to the rights of parties against a bankrupt's estate." KLEE, *supra* note 136, at 224 (discussing Pepper v. Litton, 308 U.S. 295 (1939)).

152. Blackwood, *supra* note 8, at 362.

recovery to creditors, who would otherwise have no remedy. However, the collapsing doctrine has no true legal basis in the Bankruptcy Code.[153] The collapsing doctrine reflects the same set of ideas that underlie the bankruptcy judges' restricted application of § 546(e), including the protection of small, unsophisticated creditors.

Where sentiments of equity are pertinent, it is evident that bankruptcy judges are responding to equity-based variables rather than purely legal rules and principles. There is much criticism that the characterization of bankruptcy court as courts of equity is no longer appropriate, particularly where bankruptcy courts apply a statutory scheme rather than equitable maxims and do not operate in the same fashion as true courts of equity once did.[154] As a result, federal appellate courts may, in fact, be attempting to remedy this trend,[155] justifying the application of § 546(e) and thereby exempting payments made to selling shareholders from avoidance by distinguishing results that may seem 'unfair' from those that are 'unjust.'[156] This trend among the federal appellate courts demonstrates an attempt to curb the bankruptcy courts' ability to take equitable action in situations where the Bankruptcy Code (supposedly) expresses some limited intent.[157]

C. *The Self-Regulating Market*

Another explanation for the different treatment of § 546(e) between bankruptcy judges and federal appellate judges is that the latter are pro-private market. There are two positions regarding the use of fraudulent transfer law to regulate LBOs. One position suggests that fraudulent

153. The collapsing doctrine may be justified by Bankruptcy Code § 105(a), which allows a bankruptcy court to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. §105(a) (2012). However, "[a]lthough the bankruptcy court has broad equitable power to issue orders in aid of its jurisdiction, the [Supreme] Court has limited this power when the relief granted is inconsistent with provisions of the . . . Bankruptcy Code." KLEE, *supra* note 136, at 229.

154. *See* Krieger, *supra* note 136, at 310.

155. When a "case is appealed, the upper court usually devotes its opinions to an approval or criticism of the formal-law language which was intoned by the lower court judge." Frank, *supra* note 90, at 663.

156. *See In re* Quality Stores, Inc., 355 B.R. 629, 635 n.5 (Bankr. W.D. Mich. 2006); *see also* Schilling, *supra* note 24, at 488.

157. "[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206 (1988).

transfer law need not apply in the context of an LBO because the market itself is regulation enough; the *parties can protect themselves*.[158] Some courts go so far as to suggest that if fraudulent conveyance laws are applied to LBOs indiscriminately, this acquisition method may be judicially discouraged.[159] Although federal appellate court judges have not spoken expressly about why they choose not to apply fraudulent transfer law, the fact that the LBOs are left unregulated implicitly supports the argument that these judges do not believe that regulation is necessary. On the other hand, bankruptcy decisions have outcomes consistent with the theory that the market is not sufficiently protecting unsecured creditors; bankruptcy judges do not trust the market.

The data clearly indicate that bankruptcy judges have adopted a pragmatic analysis of § 546(e) while federal appellate judges instead have adopted a purely textual analysis. This remarkable difference of interpretation demonstrates a clear departure from legal formalism. As I have demonstrated, these decisions are guided instead by the specialization of the bankruptcy courts, the recognition that bankruptcy courts are acting as courts of equity, and the attitudinal differences towards judicial regulation of the private market.

VIII. Conclusion

"In enacting and amending section 546(e) of the Bankruptcy Code, Congress has stated on numerous occasions that its purpose is to protect financial markets from the systemic risk posed by a bankruptcy [T]rustee asserting avoidance claims to unwind certain transactions that might

158. Baird and Jackson argue that creditors can protect themselves from the risk of the debtor's insolvency, "based on a conception of fraudulent conveyance law as a species of contract law." Liss, *supra* note 40, at 1511 (discussing Douglas G. Baird & Thomas H. Jackson, *Fraudulent Conveyance Law and its Proper Domain*, 38 VAND. L. REV. 829, 835-36 (1985)). This argument suggests that unsecured creditors are wholly capable of obtaining a perfected security interest, a letter of credit from the bank, or charging a fee for assuming the risk. *See id.* at 1512 ("A security interest gives the creditor the right to declare default and proceed directly against the collateral without resorting to judicial process, and assets can be appropriated to the full extent of the claim.").

159. *See, e.g.*, *In re* Morse Tool, Inc. 108 B.R. 389 (Bankr. D. Mass. 1989); *see also* Simkovic & Kaminetzky, *supra* note 9, at 137 ("[T]oo broad an application of fraudulent transfer law to these transactions would discourage useful business ventures.").

impact the markets."[160] However, as I have demonstrated, bankruptcy judges and federal appellate judges disagree fundamentally as to whether § 546(e) is limited to transactions involving financial markets. While bankruptcy judges typically interpret § 546(e) narrowly in order to prevent the apparent injustice of paying shareholders before bona fide creditors, reviewing federal appellate judges consistently interpret § 546(e) broadly, thereby shielding all stock transactions from avoidance. Although both courts use formal legal reasoning as a vehicle to explain the outcomes, the divided interpretation suggests that the decisions are justified not merely on the language of the legislation, but rather, are influenced by the specialization of the bankruptcy courts, the recognition that bankruptcy courts are acting as courts of equity, and the attitudinal differences towards judicial regulation of the private market. Legal formalism does not provide an explanation for the different outcomes.

160. Merrett & Chase, *supra* note 46.

Appendix I

§ 546(e) Does Not Apply to Protect Shareholders			**§ 546(e) Applies to Protect Shareholders**		
Bankruptcy	District	Appellate	Bankruptcy	District	Appellate
First Circuit			First Circuit		
In re Healthco Int'l, Inc., 195 B.R. 971 (Bankr. D. Mass. 1996) Autonomous	Zahn v. Yucaipa Capital Fund, 218 B.R. 656 (D.R.I. 1998)				
Second Circuit			Second Circuit		
In re Enron Corp., 328 B.R. 58 (Bankr. S.D.N.Y. 2005) Autonomous					
In re Enron Corp., 323 B.R. 857 (Bankr. S.D.N.Y. 2005) Autonomous					
In re Enron Corp., 341 B.R. 451 (Bankr. S.D.N.Y. 2006) Autonomous					
In re Norstan Apparel Shops, Inc., 367 B.R. 68 (Bankr. E.D.N.Y. 2007) Autonomous					
In re Manhattan Inv. Fund Ltd., 359 B.R.					

510 (Bankr. S.D.N.Y. 2007), *aff'd in part, rev'd in part*, 397 B.R. 1 (S.D.N.Y. 2007) Autonomous						
In re Enron Creditors Recovery Corp., 407 B.R. 17 (Bankr. S.D.N.Y. 2009), *rev'd*, 422 B.R. 423 (S.D.N.Y. 2009) Autonomous						
					In re Enron Creditors Recovery Corp., 422 B.R. 423 (S.D.N.Y. 2009)	
In re MacMenamin's Grill Ltd., 450 B.R. 414 (Bankr. S.D.N.Y. 2011) Autonomous						
						In re Enron Creditors Recovery Corp., 651 F.3d 329 (2d Cir. 2011)

					In re Quebecor World (USA) Inc., 480 B.R. 468 (S.D.N.Y. 2012)	
					AP Servs. LLP v. Silva, 483 B.R. 63 (S.D.N.Y. 2012)	
					In re Tribune Co. Fraudulent Conveyance Litig., 499 B.R. 310 (S.D.N.Y. 2013)	
				In re Tougher Indus., Inc., 2013 WL 5592902 (Bankr. N.D.N.Y. 2013) Not Autonomous		
Third Circuit				Third Circuit		
						In re Resorts Int'l, Inc., 181 F.3d 505 (3d Cir. 1999)
				In re Fin. Mgmt. Scis., Inc., 261 B.R.		

				150 (Bankr. W.D. Pa. 2001) Not Autonomous		
					In re Hechinger Inv. Co. of Del., 274 B.R. 71 (D. Del. 2002)	
In re OODC, LLC, 321 B.R. 128 (Bankr. D. Del. 2005) Autonomous				*In re* Loranger Mfg. Corp., 324 B.R. 575 (Bankr. W.D. Pa. 2005) Not Autonomous		
					In re Nat'l Forge Co., 344 B.R. 340 (W.D. Pa. 2006)	
				In re Borden Chems. & Plastics Operating Ltd. P'ship, 336 B.R. 214 (Bankr. D. Del. 2006) Not Autonomous		
				In re The IT Group, Inc., 359 B.R. 97 (Bankr. D. Del. 2006) Not Autono-		

			mous		
			In re Plassein Int'l Corp., 366 B.R. 318 (Bankr. D. Del. 2007) Not Autonomous		
				In re Plassein Int'l Corp., 388 B.R. 46 (D. Del. 2008)	
			In re Elrod Holdings Corp., 394 B.R. 760 (Bankr. D. Del. 2008) Not Autonomous		
					In re Plassein Int'l Corp., 590 F.3d 252 (3d Cir. 2009)
In re Mervyn's Holdings, LLC, 426 B.R. 488 (Bankr. D. Del. 2010) Autonomous					
	In re Appleseed's Intermediate Holdings, LLC, 470 B.R. 289 (D.				

	Del. 2012)				
In re Qimonda Richmond, LLC, 467 B.R. 318 (Bankr. D. Del. 2012) Autonomous			*In re* U.S. Mortg. Corp., 491 B.R. 642 (Bankr. D. N.J. 2013) Not Autonomous		
Fourth Circuit			Fourth Circuit		
			In re Blanton, 105 B.R. 321 (Bankr. E.D. Va. 1989) Autonomous		
			In re Derivium Capital, LLC, 437 B.R. 798 (Bankr. D. S.C. 2010) Autonomous		*In re* Derivium Capital LLC, 716 F.3d 355,(4th Cir. 2013)
Fifth Circuit			Fifth Circuit		
		Wider v. Wootton, 907 F.2d 570 (5th Cir. 1990)			
	Jewel Recovery, L.P. v. Gordon, 196 B.R. 348 (N.D. Tex. 1996)				
			In re Olympic Natural Gas Co., 258 B.R. 161 (Bankr.		

			S.D. Tex. 2001) Autonomous		
					In re Olympic Natural Gas Co., 294 F.3d 737 (5th Cir. 2002)
				Lightfoot v. MXEnergy, Inc., 2011 WL 1899764 (E.D. La. 2011)	
					In re MBS Mgmt. Servs., Inc., 690 F.3d 352 (5th Cir. 2012)
				U.S. Bank Nat'l Ass'n v. Verizon Comm. Inc., 892 F. Supp. 2d 805 (N.D. Tex. 2012)	
Sixth Circuit			Sixth Circuit		
			In re Grand Eagle Companies, Inc., 288 B.R. 484 (Bankr. N.D. Ohio 2003) Autonomous		

			In re Quality Stores Inc., 355 B.R. 629 (Bankr. W.D. Mich. 2006) Autonomous		
				QSI Holdings, Inc. v. Alford, 382 B.R. 731 (W.D. Mich. 2007)	
					In re QSI Holdings, Inc., 571 F.3d 545 (6th Cir. 2009)
Seventh Circuit			Seventh Circuit		
	Wieboldt Stores, Inc. v. Schottenstein, 131 B.R. 655 (N.D. Ill. 1991)				
			In re Renew Energy LLC, 463 B.R. 475 (Bankr. W.D. Wis. 2011) Autonomous		
			In re Lancelot Investors Fund, L.P., 467 B.R. 643 (Bankr. N.D. Ill. 2012) Autonomous		
Eighth Circuit			Eighth Circuit		

			In re Contemporary Indus. Corp., 2007 WL 5256918 (Bankr. D. Neb. June 29, 2007) Autonomous		
					Contemporary Indus. Corp. v. Frost, 564 F.3d 981 (8th Cir. 2009)
Ninth Circuit			Ninth Circuit		
			In re Comark, 124 B.R. 806 (Bankr. C.D. Cal. 1991) Autonomous		
			In re Comark, 145 B.R. 47 (B.A.P. 9th Cir. 1992) Autonomous		
					In re Comark, 971 F.2d 322 (9th Cir. 1992)
			In re Hamilton Taft & Co., 176 B.R. 895 (Bankr. N.D. Cal. 1995) Not Autonomous		
				In re Hamilton Taft	

				& Co., 196 B.R. 532 (N.D. Cal. 1995)	
					In re Hamilton Taft & Co., 114 F.3d 991 (9th Cir. 1997)
In re Grafton Partners, L.P., 321 B.R. 527 (B.A.P. 9th Cir. 2005) Autonomous					
Tenth Circuit			Tenth Circuit		
In re Republic Fin. Corp., 75 B.R. 840 (Bankr. N.D. Okla. 1987) Autonomous					
In re Kaiser Steel Corp., 105 B.R. 639 (Bankr. D. Colo. 1989), *rev'd*, 110 B.R. 514 (D. Colo. 1990) Autonomous					
					Kaiser Steel Corp. v. Charles Schwab & Co., 913 F.2d 846 (10th Cir. 1990)
					In re Kaiser

					Steel Corp., 952 F.2d 1230 (10th Cir. 1991)
	In re Kaiser Merger Litig., 168 B.R. 991 (D. Colo. 1994)				
In re Integra Realty Res., Inc., 198 B.R. 352 (Bankr. D. Colo. 1996) Autonomous					
			In re Yeagley, 220 B.R. 402 (Bankr. D. Kan. 1998) Not Autonomous		
In re D.E.I. Sys., Inc., 2011 WL 1261603 (Bankr. D. Utah April 5, 2011) Autonomous					
Eleventh Circuit			Eleventh Circuit		
In re Int'l Gold Bullion Exch., Inc., 53 B.R. 660 (Bankr. S.D. Fla. 1985) Autonomous					
		In re Munford, Inc., 98			

		F.3d 604 (11th Cir. 1996)			
In re Bankest Capital Corp., 374 B.R. 333 (Bankr. S.D. Fla. 2007) Not Autonomous					
Total Bankruptcy: 18 **Autonomous: 17** Non-Autonomous: 1 **17/27 (63%) autonomous bankruptcy court decisions held § 546(e) does NOT apply**	Total District: 5	Total Appellate: 2 2/14 (14%) appellate court decisions held § 546(e) does NOT apply	Total Bankruptcy: 20 **Autonomous: 10** Non-Autonomous: 10 **10/27 (37%) autonomous bankruptcy court decisions held § 546(e) applies**	Total District: 11	Total Appellate: 12 12/14 (86%) appellate court decisions held § 546(e) applies

Appendix II

Bankruptcy Judges

§ 546(e) Does NOT Apply to Protect Shareholders

	Bankruptcy Court	Judge (No. years practicing bankruptcy prior to decision)[1]
First Circuit		
	In re Healthco Int'l, Inc., 195 B.R. 971 (Bankr. D. Mass. 1996)	James F. Queenan, Jr. (1958-1996) 38
Second Circuit		
	In re Norstan Apparel Shops, Inc., 367 B.R. 68 (Bankr. E.D.N.Y. 2007)	Carla E. Craig (1980-1999) 19
	In re Enron Corp., 323 B.R. 857 (Bankr. S.D.N.Y. 2005)	Arthur J. Gonzalez (1983-2005) 22
	In re Enron Corp., 328 B.R. 58 (Bankr. S.D.N.Y. 2005)	Arthur J. Gonzalez (1983-2005) 22
	In re Enron Corp., 341 B.R. 451 (Bankr. S.D.N.Y. 2006)	Arthur J. Gonzalez (1983-2006) 23
	In re Enron Creditors Recovery Corp., 407 B.R. 17 (Bankr. S.D.N.Y. 2009), *rev'd*, 422 B.R. 423 (S.D.N.Y. 2009)	Arthur J. Gonzalez (1983-2009) 26
	In re Manhattan Inv. Fund Ltd., 359 B.R. 510 (Bankr. S.D.N.Y. 2007)	Burton R. Lifland (1954-2007) 53
	In re MacMenamin's Grill Ltd., 450 B.R. 414 (Bankr. S.D.N.Y. 2011)	Robert D. Drain (1985-2011) 16
Third Circuit		

1. Data obtained from Westlaw Next Profiler

	In re OODC, LLC, 321 B.R. 128 (Bankr. D. Del. 2005)	Mary F. Walrath (1979-2005) 26
	In re Mervyn's Holdings, LLC, 426 B.R. 488 (Bankr. D. Del. 2010)	Kevin Gross (1977-2010) 33
	In re Qimonda Richmond, LLC, 467 B.R. 318 (Bankr. D. Del. 2012)	Mary F. Walrath (1979-2012) 33
Fourth Circuit		
Fifth Circuit		
Seventh Circuit		
Eighth Circuit		
Ninth Circuit		
	In re Grafton Partners, L.P., 321 B.R. 527 (B.A.P. 9th Cir. 2005)	Christopher M. Klein (CJ) (1976-2005) 29
Tenth Circuit		
	In re D.E.I. Sys., Inc., 2011 WL 1261603 (Bankr. D. Utah April 5, 2011)	R. Kimball Mosier (1980-2011) 31
	In re Kaiser Steel Corp., 105 B.R. 639 (Bankr. D. Colo. 1989), *rev'd*, 110 B.R. 514 (D. Colo. 1990)	Charles E. Matheson (1961-1989) 28
	In re Integra Realty Res., Inc., 198 B.R. 352 (Bankr. D. Colo. 1996)	Patricia A. Clark (1961-1996) 35
	In re Republic Fin. Corp., 75 B.R. 840 (Bankr. N.D. Okla. 1987)	Glen E. Clark (1971-1987) 16

Eleventh Circuit		
	In re Bankest Capital Corp., 374 B.R. 333 (Bankr. S.D. Fla. 2007)	A. Jay Cristol (1959-2007) 48
	In re Int'l Gold Bullion Exch., Inc., 53 B.R. 660 (Bankr. S.D. Fla. 1985)	Sidney M. Weaver (1954-1985) 31
	Total Bankruptcy: 18	Years Total: 529/18 Average: 29.38 The average bankruptcy judge practiced bankruptcy for 29.38 years prior to issuing a decision holding that § 546(e) did not apply

§ 546(e) Applies to Protect Shareholders

	Bankruptcy Court	Judge (No. years practicing bankruptcy prior to decision)[2]
First Circuit		
Second Circuit		
	In re Tougher Indus., Inc., 2013 WL 5592902 (Bankr. N.D.N.Y. Oct. 10, 2013)	Robert E. Littlefield, Jr. (1978-2013) 35
Third Circuit		
	In re Plassein Int'l Corp., 366 B.R. 318 (Bankr. D. Del. 2007)	Kevin Gross (1978-2007) 29
	In re Elrod Holdings Corp., 394 B.R. 760 (Bankr. D. Del. 2008)	Brendan Linehan Shannon (1992-2008) 16
	In re The IT Group, Inc., 359 B.R. 97 (Bankr. D. Del. 2006)	Mary F. Walrath (1979-2006) 33
	In re Borden Chems. & Plastics Operating Ltd. P'ship, 336 B.R. 214 (Bankr. D. Del. 2006)	Peter J. Walsh (1964-2006) 42
	In re Fin. Mgmt. Scis., Inc., 261 B.R. 150 (Bankr. W.D. Pa. 2001)	Bernard Markovitz (1965-2001) 36
	In re Loranger Mfg. Corp., 324 B.R. 575 (Bankr. W.D. Pa. 2005)	Judith K. Fitzgerald (1973-2005) 32
Fourth Circuit		
	In re Blanton, 105 B.R. 321 (Bankr. E.D. Va. 1989)	Douglas O. Tice, Jr. (1957-1989) 32

2. Data obtained from Westlaw Next Profiler

	In re Derivium Capital, LLC, 437 B.R. 798 (Bankr. D. S.C. 2010)	John E. Waites (1980-2010) 30
	In re U.S. Mortg. Corp., 491 B.R. 642 (Bankr. D. N.J. 2013)	Rosemary Gambardella (1979-2013) 34
Fifth Circuit		
	In re Olympic Natural Gas Co., 258 B.R. 161 (Bankr. S.D. Tex. 2001)	William R. Greendyke (1979-2001) 22
Sixth Circuit		
	In re Quality Stores Inc., 355 B.R. 629 (Bankr. W.D. Mich. 2006)	James D. Gregg (1977-2006) 29
	In re Grand Eagle Companies, Inc., 288 B.R. 484 (Bankr. N.D. Ohio 2003)	Marilyn Shea-Stonum (1975-2003) 28
Seventh Circuit		
	In re Lancelot Investors Fund, L.P., 467 B.R. 643 (Bankr. N.D. Ill. 2012)	Jacqueline P. Cox (1978-2012) 34
	In re Renew Energy LLC, 463 B.R. 475 (Bankr. W.D. Wis. 2011)	Robert D. Martin (1969-2011) 33
Eighth Circuit		
	In re Contemporary Indus. Corp., 2007 WL 5256918 (Bankr. D. Neb. 2007)	Timothy J. Mahoney (1972-2007) 35
Ninth Circuit		
	In re Comark, 124 B.R. 806 (Bankr. C.D. Cal. 1991) *In re* Comark, 145 B.R. 47 (B.A.P. 9th Cir. 1992)	James N. Barr (1972-1991) 19 Elizabeth L. Perris (1976-1992) 16
	In re Hamilton Taft & Co., 176 B.R. 895 (Bankr. N.D. Cal. 1995)	Thomas E. Carlson (1976-1995) 19
Tenth Circuit		

	In re Yeagley, 220 B.R. 402 (Bankr. D. Kan. 1998)	John T. Flannagan (1964-1998) 34
Eleventh Circuit		
	Total Bankruptcy: 20	Years Total: 588 /20 Average: 29.40 The average appellate judge practiced bankruptcy for 29.40 years prior to issuing a decision holding that § 546(e) applied

Appendix III
Appendix III Appellate Judges

§ 546(e) Does NOT Apply to Protect Shareholders

	Appellate Court	Judge (No. years practicing bankruptcy prior to decision)[1]
First Circuit		
Second Circuit		
Third Circuit		
Fourth Circuit		
Fifth Circuit		
	Wider v. Wootton, 907 F.2d 570 (5th Cir. 1990)	Samuel D. Johnson, Jr. - 0
Seventh Circuit		
Eighth Circuit		
Ninth Circuit		
Tenth Circuit		
Eleventh Circuit		
	In re Munford, Inc., 98 F.3d 604 (11th Cir. 1996)	*Per curiam* – 0

[1]. Data obtained from Westlaw Next Profiler

	Total Appellate: 2	Years Total: 0/2 Average: 0 The average appellate judge practiced bankruptcy for 0 years prior to issuing a decision holding that § 546(e) did not apply

§ 546(e) Applies to Protect Shareholders

	Appellate Court	Judge (No. years practicing bankruptcy prior to decision)[2]
First Circuit		
Second Circuit		
	In re Enron Creditors Recovery Corp., 651 F.3d 329 (2d Cir. 2011)	John M. Walker, Jr. - 0
Third Circuit		
	In re Plassein Int'l Corp., 590 F.3d 252 (3d Cir. 2009)	Morton Ira Greenberg - 0
	In re Resorts Int'l, Inc., 181 F.3d 505 (3d Cir. 1999)	Richard Lowell Nygaard- 0
Fourth Circuit		
	In re Derivium Capital LLC, 716 F.3d 355,(4th Cir. 2013)	James Andrew Wynn Jr. - 0
Fifth Circuit		
	In re Olympic Natural Gas Co., 294 F.3d 737 (5th Cir. 2002)	Emilio M. Garza - 0
	In re MBS Mgmt. Servs., Inc., 690 F.3d 352 (5th Cir. 2012)	Edith H. Jones - 9
Sixth Circuit		
	In re QSI Holdings, Inc., 571 F.3d 545 (6th Cir. 2009)	Alan E. Norris - 0
Seventh Circuit		

2. Data obtained from Westlaw Next Profiler

Eighth Circuit		
	Contemporary Indus. Corp. v. Frost, 564 F.3d 981 (8th Cir. 2009)	Clarence Arlen Beam - 0
Ninth Circuit		
	In re Comark, 971 F.2d 322 (9th Cir. 1992)	Melvin T. Brunetti - 0
	In re Hamilton Taft & Co., 114 F.3d 991 (9th Cir. 1997)	William A. Norris – 0
Tenth Circuit		
	Kaiser Steel Corp. v. Charles Schwab & Co., Inc., 913 F.2d 846 (10th Cir. 1990)	Stephen H. Anderson - 0
	In re Kaiser Steel Corp., 952 F.2d 1230 (10th Cir. 1991)	Stephen H. Anderson – 0
Eleventh Circuit		
	Total Appellate: 12	Years Total: 9/12 Average: 0.75 The average appellate judge practiced bankruptcy for 0.75 years prior to issuing a decision holding that § 546(e) applied